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VOL. CLII NO. 228 Friday, November 20, 1987 Year

Today

THRIFTS & MORTGAGES

The British secondary mortgage market is still young, but a growing number of companies are looking to benefit from U.S. securitization techniques. 20

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They're back on the golf course in no time.

Anton R. Valukas, United States Attorney for the Northern District of Illinois, on the need for stiffer sentencing guidelines for people convicted of bank fraud. [Page 2]

Unquote

'Less Volatile' Mortgage Gains in Popularity

California Lenders Pioneer Use of Adjustable Home Loan Tied to Longer Index

By PHIL ROOSEVELT

NEW YORK — A type of adjustable-rate mortgage that has swept California appears to be gaining favor with lenders in other parts of the country.

The loans, with interest rates tied to the Federal Home Loan Bank of San Francisco's cost of funds index, are touted as less volatile than other ARMs. They already account for an estimated 75% of all California ARMs.

The loans received a further boost earlier this week when the Federal National Mortgage Association, or Fannie Mae, began a program of purchasing the loans for its portfolio.

Citing that program, First Union Mortgage Co. said it will start originating the loans from its 32-state retail network next week. First Union, based in Charlotte, N.C., is one of the nation's largest mortgage companies.

"We're going to offer it nationally," said Larry M. Dew Jr., senior vice president of First Union's residential division. "It's mainly for our California market, but we're hoping it will catch on back East, too."

Some other eastern lenders have been considering offering the loan to

THRIFTS & MORTGAGES

meet competition from western-based lenders operating in their markets.

"It's kind of a new animal in this area," said Robert J. Rocklein, senior vice president of production at Commonwealth Mortgage Co., Wellesley Hills, Mass. He added, however, that at least one California lender in New England "seems to be doing very well with it" and that Commonwealth is plotting a response.

The broadening interest in loans tied to the cost of funds index at the 11th Federal Home Loan Bank District comes as adjustable mortgages are overtaking fixed-rate loans in popularity. Some 54% of all new mortgages in September were ARMs, up from just 22% in March.

Most of the adjustable mortgages outside California, however, have been linked to indexes of U.S. Treasury securities.

The mortgage tied to the 11th district index, which was pioneered in 1981, features relatively stable interest rates, or less "payment shock"

Adjustable: Page 21

A VIEW FROM OUTSIDE

MARTIN MAYER

Exporting Money

THE MOST recent report from the Bank for International Settlements came to this country during the week the dollar teetered on the edge of the cliff. It made rather melancholy reading for those of us who believe that U.S. banks should to some degree serve American national interests — or at least not disserve them — in their international activities.

This is not the first time around for this problem. In the late 1970s, one very large U.S. bank — which I've left nameless before and will leave nameless again — added somewhat to its earnings by selling the dollar down in Hong Kong and Bahrain (there was no Tokyo market in those days), and then restoring the book to a more or less balanced condition in London and New York.

As the dollar was under pressure anyway, this daily drop at the opening tended to bring in additional sellers, so that the task of replenishment was easy.

The result, however, was a steady tendency for the dollar to close the day below the opening. Then as now, there were fools in the U.S. government who placed a higher value on flows than on stocks and thought well of a declining dollar.

But eventually even the regulators grew tired of this behavior. The Federal Reserve Board organized a couple of effective squeezes on some stretched shorts, and the Office of the Comptroller of the Currency outlined for the top management of this large New York bank just what it might mean for them over time to have the boss of the national bank examiners eager to find something wrong in their

View: Page 4

Citadel Attempts To Gain Control Of Valley Federal

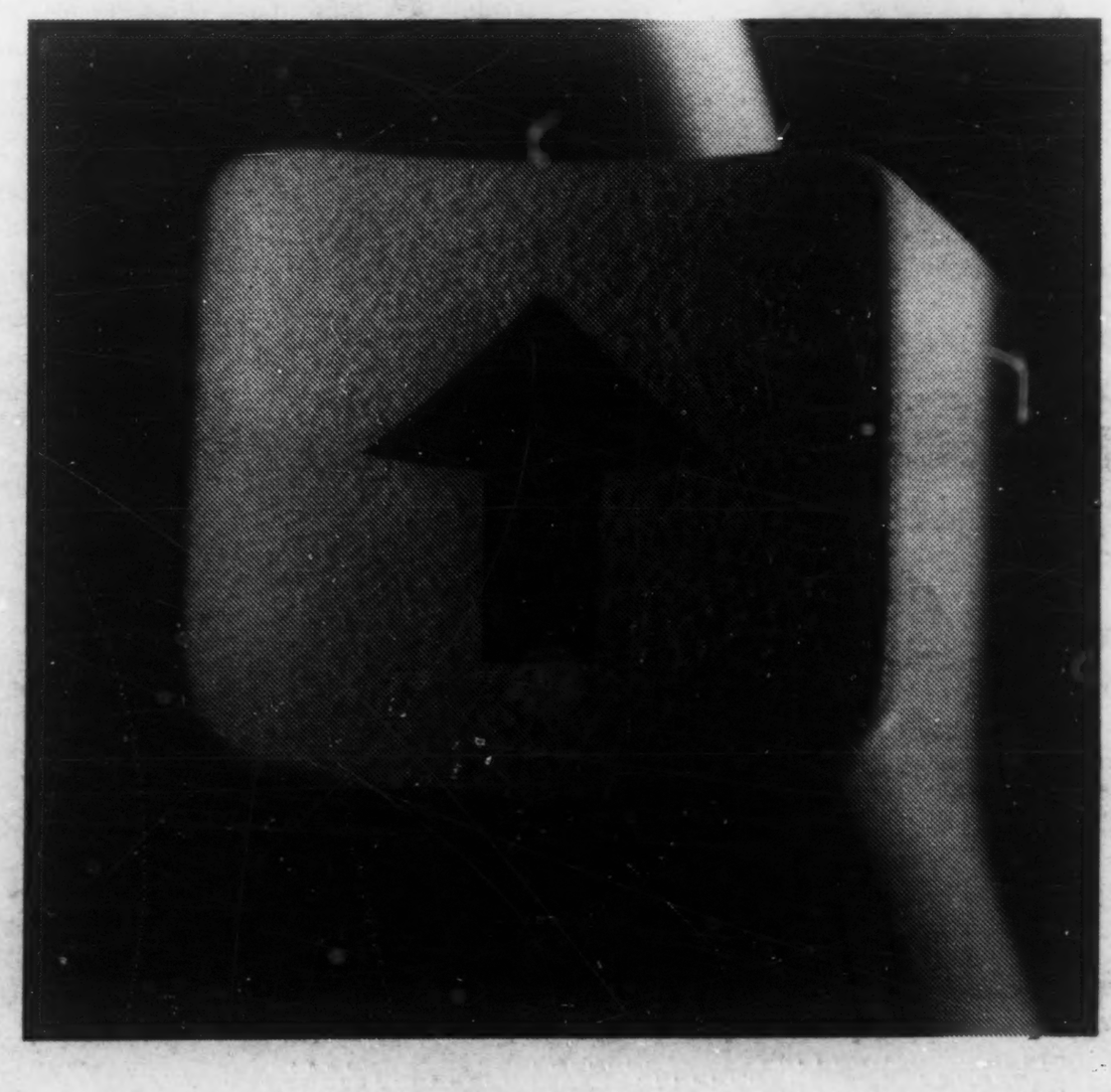
By ROBERT LUKE
West Coast Bureau

LOS ANGELES — In an apparently hostile move, Citadel Holding Corp. said it intends to acquire 32% of Valley Federal Savings and Loan Association's common shares outstanding and seek control of the thrift, which is based in Van Nuys, Calif., and has assets of $3.1 billion.

Citadel, with assets of $3.7 billion, owns no shares of Valley Federal, which operates 50 offices, chiefly in the San Fernando Valley, where Citadel's thrift subsidiary, Fidelity Federal Savings and Loan Association, also is based.

Citadel said it obtained options and a commitment to acquire the stake in

Citadel: Page 30



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Key Senators Compromise On Bank Bill

By ROBERT M. GARSSON
Washington Bureau

WASHINGTON — Legislation repealing key sections of the Glass-Steagall Act was introduced in the Senate on Thursday, following a compromise between Senate Banking Committee Chairman William Proxmire, D-Wis., and Sen. Jake Garn of Utah, the panel's ranking Republican.

Mr. Garn's willingness to cosponsor the measure was a key strategic victory for Mr. Proxmire, who appears to lack sufficient support among Democratic committee members to report out a bill. With Mr. Garn and other Republicans who would be expected to follow, Mr. Proxmire has moved a sizeable step closer to assembling the 11 votes he needs to bring the bill to the Senate floor.

"The fact that Senator Garn and Senator Proxmire have gotten together gives the bill real momentum going into early 1988," said J. Denis O'Toole, the American Bankers Association's senior Capitol Hill lobbyist. While Mr. Garn's support does not assure the bill's passage, it permits it to begin life as a bipartisan effort.

"It's too early to begin counting noses," said Karen Shaw, who follows banking legislation for the Institute for Strategy Development. "But this is now a realistic bill."

The Senate Banking Committee is expected to hold hearings Dec. 1, 2, 3, and again on Dec. 8 and 9 on the Proxmire-Garn compromise bill and others that have been introduced. The panel is not expected to begin a mark up, or vote, on the bill until next year.

While the legislation is being given reasonable odds of prevailing in the Senate, it is expected to run into a number of roadblocks on the House side. House Banking Committee Chairman Fernand J. St Germain, D-R.I., is generally thought to be hostile to a Glass-Steagall overhaul, as is Energy and Commerce Committee Chairman John D. Dingell, D-Mich.

Mr. St Germain has already begun hearings on financial services industry restructuring, as has Rep. Edward J. Markey, D-Mass., chairman of the Energy and Commerce subcommittee on telecommunications and finance.

Proxmire: Page 30 ➡

Corrections

A listing on Nov. 13 of the top 300 mortgage firms contained several errors.

California Mortgage Service, Santa Ana, understated its servicing business. The firm should have ranked as the 120th largest mortgage company, with $1.408 billion in mortgages serviced for investors on June 30, up 0.4% from a year earlier. The firm should not have been listed among those companies with the largest losses in servicing business.

Huntington Mortgage Co., Columbus, Ohio, was servicing $854.1 million for others as of June 30 and should have ranked as the 164th largest mortgage company in the nation. The company, an affiliate of Huntington Bancshares Inc., was inadvertently omitted from the listing.

BancOhio Mortgage Co., Columbus, had $721.1 million in servicing, which made it the 179th largest mortgage company at midyear. The company inadvertently omitted servicing for affiliate banks from its servicing total. This year's servicing is 7.7% higher than a year ago. Thus, the company should not have ranked among firms with the largest servicing losses. ■

CREDIT LINES

Western Union's Lenders Turn Off Spigot

By PHILIP T. SUDO

NEW YORK — The lending consortium for **Western Union Corp.** has refused to extend the company's loan commitments, citing the firm's precarious financial condition.

The commitments, which expired last week, involve a group of 31 banks, led by the Chase Manhattan Bank, Bank of America, and National Westminster Bank PLC.

The banks may now demand immediate repayment of all of Western Union's outstanding loans, approximately $227 million as of Sept. 30. Should the banks press for repayment, Western Union indicated it may file for protection under Chapter 11 of the bankruptcy code.

It was the first time the banks rejected Western Union, which has suffered

AN American Banker WEEKLY FEATURE

losses since 1983. The expired commitment, originally an override agreement reached in January 1985, consisted of three lines of credit totaling $335 million, with an additional loan of $12 million. The agreements were regularly extended every three to five months, until Nov. 13, when the last one expired.

Western Union, based in Upper Saddle River, N.J., is hopeful that the banks will accept, as part of its currently pending restructuring plan, a settlement of the debt at a substantial discount. The complex proposal calls for a merger of Western Union into its subsidiary, Western Union Telegraph Co. New York investor Bennett S. LeBow, who is seeking to acquire ITT World Communications Inc., would then fold ITT into Western Union Telegraph — if and when his acquisition is complet-

Credit Lines: Page 31 ➡

Analysts Say Foreign Banks Lag in Bonus Plans

Bank Executives at Conference Also Urged to Keep Eye on Legislative Activity

By JAMES R. KRAUS

NEW YORK — Foreign banks operating in the United States should examine incentive payments, developments in Washington, and changes in interstate banking if they want to develop a successful growth strategy, consultants advised foreign bankers at a symposium here.

Wednesday's event was organized by Peat Marwick Main & Co., the Big Eight accounting and consulting firm. Executives for the company noted that incentive payments are lagging at foreign banks and are hampering their efforts to recruit qualified personnel.

They predicted that modifications of the Glass-Steagall Act — which have now been introduced in the Senate — are likely to be limited. They warned that choosing the wrong state in which to obtain a banking charter could hamper foreign banks as interstate banking expands.

"New York's a tough place to find and retain talented people," said Daniel R. Gattis, a principal at Peat Marwick specializing in executive recruiting. The problem, said Edward R. Freher, another principal at the firm, is acute for foreign banks because their incentives lag behind those of U.S. banks. Opportunities they offer for professional advancement are also more limited.

Mr. Freher said special incentive plans are growing rapidly at U.S. banks as they expand, and these banks place a higher emphasis on profitability and cost control.

In contrast to U.S.-owned banks where estimated salary increases will average only 6.4% but incentive pay will increase, increases at foreign banks will average 7.2% but incentive pay will lag.

Peat Marwick conducted a survey on incentive pay last spring at 70 New York-based foreign banks. It indicated that only 54% of their chief lending officers were eligible for incentive pay,

Foreign Banks: Page 31 ➡

St Germain Outlines Plan to Fight Insider Abuse

By JIM McTAGUE
Washington Bureau

WASHINGTON — If banks get more powers, the agencies that regulate them should get more people to combat fraud, House Banking Committee Chairman Fernand J. St Germain, D-R.I., testified Thursday.

Rep. St Germain also said that bank privacy rights have to give way to law enforcement when a breach of trust is strongly indicated.

Rep. Doug Barnard

The House Banking Committee will draft a bill addressing the problem of privacy and insider abuse, he said. Most likely, the proposal would facilitate the transfer of customer data between banks and law enforcement officials. Now, law enforcement agencies cannot obtain any bank records without first issuing subpoenas to customers.

Mr. St Germain was one of several witnesses who discussed bank fraud before the subcommittee on commerce, consumer, and monetary affairs of the House Government Operations Committee.

Regulators Downplay Problem

Subcommittee Chairman Doug Barnard Jr., D-Ga., says bank fraud has reached "epidemic proportions." But the heads of the major banking agencies strongly disputed his claim.

"The majority of banks fail the old-fashioned way, because of a combination of poor management and economic conditions," said Robert L. Clarke, comptroller of the currency.

"We should not lose sight of the fact that most national banks are free of insider abuse. To say that insider abuse at banks is widespread or of epidemic proportions is unfair to the vast majority of men and women who routinely perform their banking functions in a safe and lawful manner," Mr. Clarke stated.

H. Robert Heller, a member of the Board of Governors of the Federal Reserve System, said most cases of criminal conduct that are referred to the Justice Department "involved relatively small sums of money that did not, in any material manner, affect the safety and soundness of financial institutions."

He noted, however, that the incidence of such crimes seems to be growing and that fraud is playing a significant role in the failure of some state banks.

L. William Seidman, chairman of the Federal Deposit Insurance Corp., said the impact of fraud on his agency has declined somewhat since 1985.

Mr. Barnard said preliminary numbers point to at least a $4.5 billion price tag for fraud at the deposit insurance funds.

St Germain Cites Failures

And Mr. St Germain said that insider abuse has played a part in one-third of the bank failures and half the collapses of savings and loans. He said he could not accept the conclusion that these cases "do not pose a threat to the stability of the system."

Other suggestions likely to come out of the hearing:

- Increased use of outside audits by commercial banks. The banking agencies are close to an agreement that would regulate the use of annual independent audits for banks with assets from $100 million to $150 million.
- Greater responsibilities for outside auditors. Mr. St Germain said he will hold hearings on independent bank auditors to explore fraud and abuse by some of those professionals.
- Greater emphasis on exchanges of criminal-investigation information between the Justice Department, the Internal Revenue Service, and the banking agencies.
- More manpower for the Justice Department to combat financial fraud.
- More judges to hear the cases.
- More use of enforcement actions by the banking agencies. In 1985 and 1986, the number of enforcement actions declined at banking agencies with the exception of the Federal Home Loan Bank Board, the subcommittee said.
- Stiffer sentencing guidelines for those convicted of bank fraud. Law enforcement officials said the robber who holds up a bank for $1,500 is likely to draw considerably more prison time than the insider who steals $15 million.

"They're back on the golf course in no time," said Anton R. Valukas, United States Attorney for the Northern District of Illinois. ■

A VIEW FROM OUTSIDE

➡ Continued from Page 1

operations.

Now, following some years of responsible behavior, the boys would seem to be at it again, en masse. After 1983, when our current account deficit began spiraling out of control, American banks became net takers of funds in the international markets. They helped the U.S. government pay the nation's bills much as the Brazilian banks helped Brazil finance its rapidly accumulating international debt until the markets closed on them in late fall 1982.

From mid-1986 to April 1987, for example, U.S. banks reduced their net creditor position — repatriated capital — by a total of $35 billion, which probably took care of a third of our current account deficit.

In the second quarter of 1987, however, American banks became again, as they had been in the dear departed years of our trade surplus, net suppliers of dollars to the world. They expanded their external assets by $8.2 billion more than the growth of their external liabilities.

This multiplied the quantity of dollars available to private parties for the purchase of marks, yen, and other foreign currencies, and thus added to the policy problems of the German, Japanese, and other central banks. In order to keep the dollar from falling through the floor in spring 1987, the central banks of Japan, the Common Market countries and, to a lesser extent, the new tigers of Asia, had to buy at least $70 billion of U.S. government paper and add it to what was already a heavy load of official holdings.

Paul Volcker's Fed had similar problems in the early 1980s, when foreign money was pouring into America. But we then refused to print new dollars and acquire instruments denominated in marks, yen, or pounds.

Instead, the Fed sterilized the inflow of funds from foreigners by reducing its own holdings of Treasury paper to hold down the money supply, keeping interest rates high enough to chloroform our inflation. After all, as the rest of the world remembers and we seem to have forgotten, we were creditors in those days, and when interest rates went up our current account improved.

Americans, unfortunately, still don't see that what they call "diversifying abroad" — when they do it — is indistinguishable from what they call "capital flight" — when it is done by people whose native language is not English.

Because they could see the proceeds of official loans to this country returning to their shores in the form of private acquisitions of their assets, Japan and the Common Market countries became increasingly reluctant to maintain the patterns of their lending to us. As they began to sterilize the inflow of funds, their interest rates began to rise. Ours had to follow, with the results we have seen.

Ways to handle this problem are not easy to find. Even if we wished to impose exchange controls, we couldn't make them work.

And what foreign exchange business our banks didn't do if we kept them from exporting money, other people's banks would pick up soon enough. Still, we will have to find some way to discourage the sort of thing that happened in 1978-79 and again in the second quarter of 1987.

Perhaps our old friend disclosure could help. Why not include in the call reports, and make the information publicly available, a quarterly statement of the net import or export of dollars by each bank?

Then customers who have reason to fear a whirlpool of decline in the dollar will be able to exert a little private-sector suasion on their banks. And the Treasury, which now has this jug-eared, toothy, what-me-worry look whenever anyone talks about the dollar, might learn what's going on. ■

Mr. Mayer is the author of "The Bankers" and "The Money Bazaars."

It is still as true as it was in George

Washington's day . . . that nations do not have permanent friends or enemies, only permanent interests.

IN THE SECOND quarter of 1987, the Germans and Japanese decided by contrast that they would permit the inflow of funds from America to enlarge their money supply, keeping their interest rates well below U.S rates, at least for the time being. By inflating their currencies, they made it possible for the Fed to hold down the growth of M-1 in the United States, which had been clearly excessive for the preceding year.

It is still as true as it was in George Washington's day, of course — especially in the economic sphere — that nations do not have permanent friends or enemies, only permanent interests. Our trading partners were giving us this assistance in large part because they were hooked on exporting to us, and we could not import unless they lent us the money to do so.

Still, they were being helpful, and they certainly deserved better thanks than the denunciation they got from Treasury Secretary James A. Baker 3d. He insisted that they had failed to live up to their obligations under the Louvre agreement because they were not stimulating their economies.

But most economic theories — including those espoused by the present chairman of the Council of Economic Advisors — argue that what our trading partners did with their money supply in the second quarter was highly, indeed dangerously stimulative of their own economies.

The last time these countries permitted the United States to cast them in the role of "locomotive," in 1978-79, we saw a worldwide inflation that was very painful to extinguish.

The Germans and Japanese are not necessarily wrong to remember experiences less than 10 years old, and we are not necessarily right to forget them. And we are certainly wrong to hector these people about the need to keep interest rates low only five years after our Federal Reserve drove the short-term rates the world pays on its debt to 14%-15%.

Such disputes have been with us a while, and it has not been entirely clear what brought them to a head this summer and early fall. The data from the Bank for International Settlements may provide an explanation.

LIKE WATER RUNNING uphill, private money in the second quarter moved from a high-interest-rate to a low-interest-rate environ-

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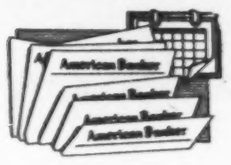
Remember, we need your views to be a true community newspaper.

FLASHBACKS

What made news in the *American Banker* this week...



50 Years Ago

• A coin purported to be a 1913 Liberty Head nickel, found by a 13-year-old Texas boy, was called a probable forgery by coin experts. Although a die was cast for a 1913 Liberty Head nickel and several trial coins were later struck and sold to collectors, the Buffalo nickel was designed and distributed that year. Experts speculated the coin found in Texas was a forgery of a 1903 nickel, done by skilled engravers.

• J.P. Morgan returned to New York aboard the Queen Mary following his annual goose-hunting vacation at his lodge in Scotland. Upon his arrival, he declined to answer questions about the stock market, taxes, or politics. "I have nothing to say and I am going to say it," he told reporters.

• An adviser for the World's Fair in New York told New Jersey banks that the show would open, on schedule, on April 30, 1939. Kenneth M. Murchison, formerly the vice president of the Central Savings Bank of New York, said "a lot of visitors may not like the so-called functionalism of the architectural style and may sigh for the grandeur of Chicago's 1983 Columbian Exposition, but I am sure that New Yorkers are going to be proud of their 'World of Tomorrow.' "

20 Years Ago

• A tighter monetary policy was expected from the Federal Reserve Board after the weekend devaluation of the British pound. Eli Shapiro, professor of finance at Harvard University, said the Fed no longer had to worry about the effect a tighter monetary policy would have on the pound. "Instead," he told bankers in Chicago, "they are more concerned with protecting the dollar now that the pound has been devalued."

10 Years Ago

• New York State Lieutenant Gov. Mary Anne Krupsak told a Savings Bank Association conference, "If you're interest in getting more savings from people, you yourselves should start to pay women salaries equal to what you pay men for comparable work." Citing recent class-action suits, Ms. Krupsak said, "It will be cheaper for you to raise salaries and start training programs voluntarily."

• President Carter signed legislation extending for one year deposit rate ceilings that had been in effect since 1966. Regulation Q, as the statute was known, was due to expire Dec. 15. It was used by federal agencies to limit savings rate and to give thrifts a competitive advantage in attracting deposits.

5 Years Ago

• President Reagan became the first President to address the U.S. League of Savings Institutions. "Your industry faced chaos in 1980," he told thrift executives meeting in New Orleans, but said his economic program was "beginning to do exactly what it was intended to do. The sun is shining on thrifts again."

• In an unprecedented meeting held on short notice, officials of the International Monetary Fund urged representatives of 18 international banks to maintain or increase their lending to Mexico and Argentina to tide them over credit difficulties.

• C.T. Conover, the comptroller of the currency, told the American Bankers Association's conference of chief financial officers that country lending limits might be placed on banks in light of concern over loans to lesser-developed nations. He said that while his agency was not developing such limits, he expected Congress would act on the matter.

1 Year Ago

• United Oklahoma Bankshares Inc. applied for open-bank assistance from the Federal Deposit Insurance Corp. for its Oklahoma City subsidiary. The application sought assistance for the United Oklahoma Bank, Oklahoma City, according to the holding company's quarterly public disclosure report submitted to the Securities and Exchange Commission.

— Domenica Trevor